

Message Text

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ACTION EUR-12

INFO OCT-01 EA-12 IO-14 ISO-00 AID-05 CIAE-00 EB-08
FRB-01 INR-10 NSAE-00 ICA-20 XMB-04 OPIC-06 SP-02
LAB-04 SIL-01 OMB-01 PA-02 NSC-05 SS-15 STR-07
CEA-01 ABF-01 /132 W
-----009595 031902Z /50

P R 031759Z MAY 78
FM AMEMBASSY LONDON
TO SECSTATE WASHDC PRIORITY 5758
TREASURY DEPT WASHDC PRIORITY
INFO AMEMBASSY BONN
AMEMBASSY BRUSSELS
AMEMBASSY DUBLIN
AMEMBASSY PARIS
AMEMBASSY ROME
AMEMBASSY TOKYO
AMCONSUL BELFAST
AMCONSUL EDINBURGH
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USEEC ALSO FOR EMBASSY
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DEPARTMENT PASS FEDERAL RESERVE BOARD; TREASURY FOR
DONALD E. SYRUD, OASIA

E.O. 11652: N/A
TAGS: ECON, UK
SUBJECT: ECONOMIC DEVELOPMENTS FOR PERIOD APRIL 27 MAY 3

SUMMARY: THE FINANCIAL TIMES SURVEY OF BUSINESS OPINION
SHOWS BUSINESS OPTIMISM WANING. OFFICIAL RESERVES, AS
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EXPECTED, FELL A RECORD 3.3 BILLION DOLLARS. SHORT-TERM
INTEREST RATES WERE UNDER UPWARD PRESSURE BUT DID NOT
AFFECT LONGER YIELDS. STERLING STRENGTHENED DURING THE
WEEK BUT APPEARS TO HAVE NO UPWARD MOMENTUM. END SUMMARY

1. FINANCIAL TIMES BUSINESS SURVEY. BUSINESS OPINION
HAS BECOME MORE CAUTIOUS ABOUT THE GENERAL ECONOMIC CLI-

MATE SINCE THE BEGINNING OF THE YEAR. ACCORDING TO MONTHLY SURVEY PUBLISHED BY THE FINANCIAL TIMES, RESPONDENTS EXPRESSING OPTIMISM ABOUT THEIR FIRM'S PROSPECTS IN THE COMING YEAR DROPPED FROM 42 TO 37 PERCENT BETWEEN JANUARY AND APRIL. THERE WAS A CORRESPONDING RISE FROM 15 TO 25 PERCENT OF FIRMS TAKING A LESS OPTIMISTIC VIEW. PROFIT MARGINS ARE EXPECTED TO COME UNDER PRESSURE BY A THIRD OF RESPONDENTS COMPARED WITH ONLY 21 PERCENT IN JANUARY. MOST FIRMS EXPRESSED THE VIEW THAT THE APRIL BUDGET WOULD NOT HAVE MUCH INFLUENCE ON THEIR OWN SITUATIONS. OTHER ELEMENTS IN THE SURVEY INDICATE THAT

- EXPORT PROSPECTS AND NEW ORDERS ARE LITTLE CHANGED FROM LAST JANUARY;
- INVENTORY LEVELS ARE LIKELY TO DECLINE SLOWLY IN THE COMING YEAR;
- WEAK DEMAND REMAINS THE MAIN CONSTRAINT ON OUTPUT, THOUGH SHORTAGES OF SKILLED FACTORY STAFF, AND EXECUTIVES ARE BEING CITED BY A GROWING MINORITY OF FIRMS;
- INVESTMENT PROSPECTS REMAIN RELATIVELY HEALTHY;
- LABOR COSTS ARE EXPECTED TO RISE BETWEEN 12 AND 13 PERCENT IN THE COMING YEAR WHILE UNIT COSTS ARE LIKELY TO INCREASE BY ABOUT 11 PERCENT.

2. OFFICIAL RESERVES FELL 3282 MILLION DOLLARS DURING APRIL TO 17,038 MILLION DOLLARS. DURING THE MONTH, THE PUB
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LIC SECTOR BORROWED 76 MILLION DOLLARS UNDER THE EXCHANGE COVER SCHEME. A 943 MILLION DOLLAR EARLY REPAYMENT TO THE IMF, AND 300 MILLION DOLLARS IN OTHER EARLY REPAYMENTS WERE MADE DURING THE MONTH AS WELL. THE OFFICIAL RESERVES THUS SUFFERED AN UNDERLYING DECLINE OF 2,115 MILLION DOLLARS OVER THE MONTH.

THE RECORD FALL IN RESERVES WAS SLIGHTLY LARGER THAN MARKET SOURCES HAD EXPECTED BUT WAS CLOSE ENOUGH TO THE ANTICIPATED DECLINE TO RUFFLE NEITHER THE FINANCIAL NOR THE FOREIGN EXCHANGE MARKETS. MARKET SOURCES HAVE NOTED THAT THE BANK OF ENGLAND HAS COUNTERED HEAVY SELLING PRESSURE ON STERLING WITH LARGE AND HIGHLY VISIBLE INTERVENTION THIS MONTH.

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CEA-01 ABF-01 /132 W
-----009620 031902Z /50

P R 031759Z MAY 78
FM AMEMBASSY LONDON
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3. THE MONEY MARKETS WERE VERY ACTIVE DURING THE WEEK AS SHORT-TERM INTEREST RATES ROSE SHARPLY. AT FRIDAY'S TREASURY BILL AUCTION, BIDS DID NOT EXCEED THE TENDER BY AN APPRECIABLE AMOUNT, AND THE AVERAGE TREASURY BILL RATE WAS VERY CLOSE TO INDICATING A QUARTER PERCENT RISE IN THE MINIMUM LENDING RATE (MLR). MARKET SOURCES SAY THAT MANY EXPECT MLR TO REACH 8-1/2 TO 9 PERCENT, ALTHOUGH THEY DON'T EXPECT SUCH A SHARP JUMP THIS WEEK.

GILT MARKET PRICES ON THE OTHER HAND DID NOT MOVE APPRECIABLY AND VOLUME WAS SMALL DURING THE WEEK. MARKET
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SOURCES DO NOT BELIEVE THAT ANY SIGNIFICANT QUANTITY OF THE NEW GILT WAS PURCHASED AT LAST THURSDAY'S APPLICATION. THE RISE IN SHORT-TERM INTEREST RATES IS SAID TO HAVE BEEN DISCOUNTED IN GILT PRICES.

4. A. STERLING WHILE STRENGTHENING DURING THE WEEK, AP-

PEARS TO BE IN A HOLDING PATTERN. THE DROP IN RESERVES ANNOUNCED TODAY WAS EXPECTED AND DISCOUNTED. AN INCREASE IN MLR IS ANTICIPATED. THE BANK OF ENGLAND WAS SEEN IN THE MARKET SUPPORTING THE RATE LAST WEEK, BUT NOT THIS WEEK. THE BANK WAS ALSO CONSIDERED TO HAVE BEEN OPERATING IN SHORT-DATED FORWARDS TO SUPPORT SPOT, AND TO DELIBERATELY SQUEEZE SPECULATORS; THEREBY MAKING DEALERS SOMEWHAT RELUCTANT TO RUN OPEN POSITIONS. AS STERLING APPROACHED THE \$1.83 LEVEL THIS WEEK, THERE HAVE BEEN SIGNS OF FAIRLY SIZEABLE COMMERCIAL SELLING OF STERLING.

B. THE MARKET IS ALSO DIGESTING APPARENTLY INSPIRED PRESS ARTICLES (SEE P. 1 OF FINANCIAL TIMES, MAY 2) THAT THE GOVERNMENT'S AIM IS TO KEEP THE STERLING EXCHANGE RATE BROADLY STABLE AT ABOUT PRESENT LEVELS FOR THE TIME BEING; IF TRUE, MOST MARKET OPERATORS CONSIDER THIS MEANS SOME COMBINATION OF INTEREST RATES RISING FURTHER, AND THE BANK SPENDING MORE RESERVES TO DEFEND THE RATE.

C. SOME FOREX DEALERS CONSIDER (AS REPORTED LAST WEEK, PARA. 5 C., LONDON 6637) THAT STERLING'S NEXT MAJOR TEST MAY BE ON MAY 15 WHEN APRIL TRADE FIGURES ARE ANNOUNCED. THEY REPORT SOME, BUT NOT MUCH, SELLING OF STERLING BY FOREIGN INVESTORS. THE UNDERLYING UNCERTAINTIES REMAIN -- INCLUDING CURRENT ACCOUNT TRENDS AND THE BUDGET/MONETARY POLICY INTERPLAY. WITH THE DOLLAR STRENGTHENING, SOME BELIEVE STERLING COULD BECOME THE WEAK LINK IN THE CHAIN; IN THE SHORT-TERM, HOWEVER, THE MARKET EXPECTS THE GOVERN-
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MENTFOR POLITICAL AND COUNTER-INFLATIONARY REASONS TO SUPPORT THE RATE.

5. EXCHANGE RATE AND GOLD EFFECTIVE

EXCHANGE RATE			
DATE	EXCHANGE RATE (\$)	(DEC. 1971 EQUALS 100)	GOLD (\$)
4/26	1.8145	61.2	168-3/8
4/27	1.8330	61.4	170-5/8
4/28	1.8245	61.4	170-5/8
5/1	MARKETS CLOSED		
5/2	1.8265	61.6	169-1/8
CHANGE 4/25-5/2 UP 0.0115 UP 0.4 UP 1-1/4			

6. FORWARD PREMIUM ON STERLING

DATE	1 MONTH	3 MONTHS	6 MONTHS
4/26	- 0.50	- 1.20	- 2.20
4/27	- 0.45	- 1.30	- 2.40
4/28	- 0.45	- 1.17	- 2.17
5/1	MARKETS CLOSED		
5/2	- 0.42	- 1.12	- 2.27

CHANGE 4/25-5/2 UP 0.06 DOWN 0.17 DOWN 0.54
(ALL FIGURES IN CENTS)

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P R 031759Z MAY 78
FM AMEMBASSY LONDON
TO SECSTATE WASHDC PRIORITY 5760
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7. EURODOLLAR INTEREST RATES

DATE	1 MONTH	3 MONTHS	6 MONTHS
4/26	6-7/8	7-3/8	7-7/8
4/27	7-3/4	7-5/8	7-7/8
4/28	7-3/8	7-3/4	8
5/1	MARKETS CLOSED		
5/2	7-3/8	7-7/8	8

CHANGE 4/25-5/2 UP 1/8 UP 3/8 UP 1/8

8. THREE-MONTH LONDON INTERBANK - EURODOLLAR INTEREST
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RATE DIFFERENTIAL

DATE	
4/26	13/16
4/27	23/32
4/28	19/32
5/1	MARKETS CLOSED
5/2	13/16
CHANGE 4/25-5/2	UP 9/32

9. STERLING CERTIFICATES OF DEPOSIT

DATE	1 MONTH	3 MONTHS	6 MONTHS
4/26	7-17/32	8-1/16	8-7/16
4/27	7-23/32	8-5/32	8-9/16
4/28	7-21/32	8-3/16	8-19/32
5/1	MARKETS	CLOSED	
5/2	7-25/32	8-5/8	8-15/16
CHANGE 4/25-5/2	UP 1/2	UP 23/32	UP 5/8

10. INTERPOLATED REDEMPTION YIELDS OF HIGH COUPON GOVERNMENT SECURITIES

DATE	5 YEARS	15 YEARS	25 YEARS
4/26	11.02	12.68	12.95
4/27	11.02	12.68	12.96
4/28	10.94	12.67	12.98
5/1	MARKETS	CLOSED	
5/2	10.99	12.67	13.00
CHANGE 4/25-5/2	UP 0.04	UP 0.03	UP 0.08

11. THE MINIMUM LENDING RATE REMAINED 7-1/2 PERCENT AFTER FRIDAY'S TREASURY BILL AUCTION SAW THE AVERAGE TREASURY BILL RATE RISE BUT .0312 PERCENT TO 6.9988 PERCENT. THE 500 MILLION POUNDS IN BILLS TENDERED ATTRACTED 594.88 MILLION POUNDS IN BIDS. THIS WEEK 500 MILLION POUNDS IN

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BILLS WILL AGAIN BE OFFERED AS 300 MILLION POUNDS MATURE.

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Message Attributes

Automatic Decaptioning: X
Capture Date: 01 jan 1994
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Draft Date: 03 may 1978
Decaption Date: 01 jan 1960
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Disposition Approved on Date:
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Disposition Date: 01 jan 1960
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Disposition Reason:
Disposition Remarks:
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Handling Restrictions: n/a
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Legacy Key: link1978/newtext/t19780598/aaaadfov.tel
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Subject: ECONOMIC DEVELOPMENTS FOR PERIOD APRIL 27 MAY 3 SUMMARY: THE FINANCIAL TIMES SURVEY OF BUSINESS OPINION SHOWS BUSINESS OPTIMISM WANING. OFFICIAL RESERVES
TAGS: ECON, UK
To: STATE TRSY
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